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No. 256

Supreme Court of the United States

OCTOBER TERM, 1942

WILGARD REALTY COMPANY, INC.,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

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CITATIONS

In the Supreme Court of the United States

October Term, 1942

No.

Wilgard Realty Company, Inc.,
Petitioner,
v.
Commissioner of Internal Revenue,
Respondent.

PETITION FOR WRIT OF CERTIORARI

TO THE HONORABLE THE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The petitioner prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered April 29, 1942 (R. 49).

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 28-38) is reported in 43 B.T.A. 557. The opinion of the Circuit Court of Appeals (R. 49-55) is reported in 127 F. 2d 514.

JURISDICTION

The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Where taxpayer sustained a loss upon the voluntary sale of its real property in 1937, can Congress, by Section 213 (f) of the Revenue Act of 1939, constitutionally change the basis of the property, so as to convert taxpayer's prior loss into a gain and impose a tax thereon more than two years after the consummation of the sale?

STATUTES INVOLVED

The pertinent statutory provisions are set forth in the Appendix, *infra*, pp. 8-11.

STATEMENT

The petitioner was organized and incorporated under the laws of New York State on August 12, 1932, with an authorized capital stock of 200 common shares of no par value. On August 16th following, W. H. H. Chamberlin, an individual, conveyed to petitioner certain business property located in Syracuse, N. Y., in consideration for petitioner's issuance to Chamberlin of its authorized capital stock, with the exception of three shares of the incorporators, and in further consideration of the agreement by petitioner to pay two mortgages on the property in the principal sum of $35,000. Immediately upon the issuance of the stock to Chamberlin, he divested himself of control of the petitioner corporation by making gifts of about four-fifths of his newly acquired shares. (R. 26)

At the time of the conveyance of the real property to petitioner, the basis of the property in the hands of Chamberlin, the transferor, was its fair market value on March 1, 1913, which was, after adjustment for depreciation, $65,041.67. (R. 27)

On February 18, 1937, the petitioner sold the property for $19,000 cash, and the purchaser assumed and agreed to pay the two mortgages still remaining unpaid in the principal sum of $35,000. From the date of petitioner's acquisition of the property to the date of its sale, depreciation was allowed and allowable in the amount of $8,475. The expense of the sale was $3,925.04. Petitioner was voluntarily dissolved on July 13, 1937. (R. 27)

The petitioner takes the position that the maximum $2000 capital loss deduction was properly made in its 1937 Income and Excess Profits Tax Return, since the property acquired a new basis in 1932 when the petitioner assumed the transferor's mortgage obligations ($65,041.67 plus $35,000); that the subsequent sale of the property in 1937 resulted in a loss of $41,491.71 determined on such basis; and that Congress, by Section 213 (f) of the Revenue Act of 1939, cannot retroactively withdraw the basis acquired by the property in 1932, so as to convert into a gain the loss sustained upon the sale of the property in 1937, and thus create a new tax liability more than two years after the sale.

The respondent claims that such retroactive legislation is not repugnant to the due process clause of the Fifth Amendment and that therefore the 1937 sale of petitioner's property may be reopened two years later, a new basis substituted for determining gain or loss, a

gain of $15,075.02 computed on the substituted basis, and a deficiency of $2,716.23 assessed.

REASONS FOR GRANTING WRIT

The Circuit Court of Appeals has here decided an important question of federal and constitutional law which has not been, but should be, settled by this Court. The case presents for the first time the question of the constitutionality of Section 213 (f) of the Revenue Act of 1939, which, the petitioner maintains, effects a denial of due process. In support of its application herein the petitioner advances the following argument.

When the petitioner sold its real property on February 18, 1937, it voluntarily changed its position. In so doing, it sustained a capital loss under the law of the land then in effect, namely, Sec. 113 (a) (8), Revenue Act of 1936, and Sec. 112 (b) (5), Revenue Act of 1932. On March 28, 1938, this Court in *United States* v. *Hendler*, 303 U. S. 564, interpreted the said statutory provisions as allowing a loss such as claimed by the present petitioner. On June 29, 1939, the Revenue Act of 1939 became law; incorporated therein was Section 213 (f), the legislative intent of which was to nullify the effect of the provisions of prior revenue acts as construed in the *Hendler* decision.* The effect of Section 213 (f), as applied in the case at bar, is to convert into a gain the loss sustained by the petitioner on a sale made more than two years before the passage of the Act, and to tax the asserted gain.

The petitioner has no quarrel with the legislative custom of making an income-taxing statute retroactive

*76th Cong., 1st sess., House Rept. No. 855, pp. 5, 18-20; Cong. Rec., vol. 84—part 7, pp. 7481-2.

to the beginning of the taxable year in which it is enacted (*United States* v. *Hudson*, 299 U. S. 498, 500); nor does the petitioner here challenge the power of Congress merely to change the basis of property acquired in prior years for purposes of *prospective* taxation. But the petitioner does take its stand on the proposition that Congress cannot constitutionally reconstruct the pattern of prior revenue laws so as to levy a tax, where none existed before on a transaction consummated, as here, more than two and one-third years before the date of enactment. Although this retroactive period would appear grossly excessive, Section 213 (f) could by its terms operate to tax a transaction completed *more than four years* prior to the enactment of the Revenue Act of 1939.*

When the petitioner sold its real property in 1937, it voluntarily changed its position, much as does a donor who transfers his assets by gift. In the latter instance, this Court has held that the levying of a new tax upon a gift completed in the past would be so oppressive as to violate due process, since the donor could not have elected whether or not to make the gift in the light of the unforeseen tax. (*Nichols* v. *Coolidge*, 274 U. S. 531; *Blodgett* v. *Holden*, 275 U. S. 142; *Untermyer* v. *Anderson*, 276 U. S. 440; *Coolidge* v. *Long*, 282 U. S. 582;

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*Thus, where a sale at a loss had been consummated in May, 1935, a taxpayer on the basis of a fiscal year ending April 30th would report such loss in his return due July 15, 1936; the statute of limitations would not yet have run against the Commissioner when the Revenue Act of 1939 became law on June 29, 1939, and hence the Act by its terms permits the taxing of a transaction completed more than four years prior to its enactment!

Helvering v. *Helmholz*, 296 U. S. 93; *White* v. *Poor*, 296 U. S. 98.) By parity of reasoning in the present case, a new tax liability may not be retroactively imposed on a completed capital transaction such as a sale—a change of position no less voluntary than if resulting from a gift. Thus, the Court of Appeals for the District of Columbia has indicated that the rule established in the gift cases would invalidate a tax on transactions for profit consummated in a prior year (*Neild* v. *District of Columbia*, 110 F. 2d 246, 253).

The Court below ultimately rests its decision (R. 55) upon the supposition that both parties to the 1932 exchange then believed erroneously that such transaction was tax-free, and that therefore the present petitioner is not legally harmed by the challenged statute which merely conformed the law with their alleged belief. However, there is a total absence of evidentiary support in the stipulated facts (R. 25-27) for such an inference; and, even assuming *arguendo* the correctness of the inference, the Court's legal conclusion does not follow. Whatever interpretation was put upon the exchange transaction by Chamberlin, the individual transferor, his views of the law in no wise bound his transferee, the present petitioner. Chamberlin, it will be recalled, divested himself of control of the petitioner corporation immediately following the exchange (R. 26), and was thereafter a mere minority stockholder. In every tax return filed by the petitioner throughout its existence, it evaluated its real property on the theory of a new stepped-up basis acquired in 1932, and otherwise conducted itself in a manner entirely consistent with its present position. It is difficult to see what more the petitioner was re-

quired to do in order to apprise the Commissioner that it at all times treated the basis of the real property as increased after the exchange. To deny the petitioner relief on the theory that it is forever bound by an alleged mistake of law on the part of its transferor is a manifest injustice. And to permit the imposition of a tax on capital transactions completed in prior years violates the spirit of fair play which under the Constitution should mark the relations between taxpayers and their Government.

WHEREFORE, in order to have the important question of federal and constitutional law appearing herein settled by this Court, the petitioner respectfully prays that a writ of certiorari may be issued directed to the United States Circuit Court of Appeals for the Second Circuit, commanding said Court to certify and send to this Court, on a day certain, a complete transcript of the record and proceedings of said Circuit Court of Appeals in this case entitled "*Wilgard Realty Company, Inc.* v. *Commissioner of Internal Revenue*, October, 1941, Term, No. 44," to the end that said case may be reviewed and determined by this Court as provided by law, and that the petitioner may have such other and further relief as to this Court may seem appropriate, and that the judgment of the Circuit Court of Appeals may be reversed by this Honorable Court.

Respectfully submitted,

WILGARD REALTY COMPANY, INC.

By HENRY S. FRASER,
DAVID A. FRASER,
Attorneys for Petitioner.

JULY 24, 1942.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

*   *   *   *   *

(c) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

*   *   *   *   *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges solely in kind.*—

*   *   *   *   *

(5) *Transfer to corporation controlled by transferor.*—No gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock or securities in such corporation, and immediately after the exchange such person or persons are in control of the corporation; but in the case of an exchange by two or more persons this paragraph shall apply only if the amount of the stock and securities received by each is substantially in proportion to his interest in the property prior to the exchange.

(c) *Gain from exchanges not solely in kind.*—

(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5) of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain, but also

of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of gain or loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) *Amount realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

* * * * *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (unadjusted) of property.*—The basis of property shall be the cost of such property; except that—

* * * * *

(8) *Property acquired by issuance of stock or as paid-in surplus.*—If the property was acquired after December 31, 1920, by a corporation—

(A) by the issuance of its stock or securities in connection with a transaction described in section 112 (b) (5) (including, also, cases where part of the consideration for the transfer of such property to the corporation was property or money, in addition to such stock or securities), or

(B) as paid-in surplus or as a contribution to capital,

then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made.

Revenue Act of 1939, c. 247, 53 Stat. 862:

SEC. 213. ASSUMPTION OF INDEBTEDNESS.

*   *   *   *   *

(f) *Assumption of liability not recognized under prior acts.*—

(1) Where upon an exchange occurring in a taxable year ending after December 31, 1923, and beginning before January 1, 1939, the taxpayer received as part of the consideration property which would be permitted by subsection (b) (4) or (5) of section 112 of the Revenue Act of 1938, or the corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts, to be received without the recognition of gain if it were the sole consideration, and as part of the consideration another party to the exchange assumed a liability of the taxpayer or acquired from the taxpayer property subject to a liability, such assumption or acquisition shall not be considered as "other property or money" received by the taxpayer within the meaning of subsection (c), (d), or (e) of section 112 of the Revenue Act of 1938, or the corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts, and shall not prevent the exchange from being within the provisions of subsection (b) (4) or (5) of section 112 of the Revenue Act of 1938, or the corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts; except that if, in the determination of the tax liability of such taxpayer for the taxable year in which the exchange occurred, by a decision of the Board of Tax Appeals or of a court which became final before the ninetieth day after

the date of enactment of the Revenue Act of 1939, or by a closing agreement, gain was recognized to such taxpayer by reason of such assumption or acquisition of property, then for the purposes of section 112 of the Revenue Act of 1938, and corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts, such assumption or acquisition (in the amount of the liability considered in computing the gain) shall be considered as money received by the taxpayer upon the exchange.

(2) Paragraph (1) shall be effective with respect to the Revenue Act of 1924 and subsequent revenue Acts as of the date of enactment of each such Act.

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CITATIONS

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In the Supreme Court of the United States

OCTOBER TERM, 1942

No. 256

WILGARD REALTY COMPANY, INC., PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax appeals (R. 28–38) is reported at 43 B. T. A. 557. The opinion of the Circuit Court of Appeals (R. 49–54) is reported at 127 F. (2d) 514.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on May 15, 1942. (R. 54.) The petition for a writ of certiorari was filed July 27, 1942. The jurisdiction of this Court is invoked

under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The petitioner acquired some realty from an individual in 1932 in exchange for its capital stock and the assumption of outstanding mortgages on the property. That exchange was made non-taxable by Section 112 (b) (5) of the Revenue Act of 1932, as amended by Section 213 (f) of the Revenue Act of 1939, and as a consequence the petitioner was required to take the transferor's basis under Section 113 (a) (8) of the Revenue Act of 1936. In 1937 the petitioner sold this realty.

The sole question presented is whether Section 213 (f) of the 1939 Act is constitutional as applied here, since it keeps the 1932 exchange within Section 112 (b) (5) despite the assumption of the mortgages and thus prevents the realty from acquiring a "stepped-up" basis.

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra*, pp. 9–14.

STATEMENT

The facts, as stipulated (R. 25–27) and found by the Board (R. 29–30), may be stated as follows:

The petitioner, a New York corporation organized on August 12, 1932, by one Chamberlin, acquired certain realty from Chamberlin on August

16, 1932,[1] in consideration of the issuance to him of practically all its capital stock and its assumption of mortgages outstanding on the property in the principal amount of $35,000. The remaining three shares of petitioner's stock, which had been issued to the incorporators, had, in the meantime, been acquired by Chamberlin at $1 per share, so that immediately after the exchange Chamberlin owned all of the petitioner's stock. Shortly thereafter, he made gifts of about four-fifths of the stock to members of his family. (R. 26, 29–30.)

The basis of the property in the hands of Chamberlin at the time of the transfer to petitioner was its fair market value on March 1, 1913 ($65,-041.67. See R. 27.), which, after adjustment for depreciation to August 15, 1932, was $43,474.94.[2] The fair market value of the property on August 16, 1932, was $110,000. (R. 30.)

On February 18, 1937, the petitioner sold the property for $19,000 in cash and the purchaser assumed the mortgages on the property, the unpaid principal of which still amounted to $35,000. From the date of the acquisition of the property by petitioner to the date of its sale, depreciation was allowed and allowable in the amount of $8,475. The expense of the sale was $3,925.04. (R. 30.)

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[1] The date of that transfer appears erroneously as August 12 in the course of the Board's opinion, instead of August 16 as stipulated by the parties. (See R. 26; cf. R. 2, 39–40.)

[2] The amount of depreciation between March 1, 1913, and August 15, 1932, appears in the Commissioner's computation (R. 20), and has not been contested.

In its income tax return for 1937, the petitioner reported the sale as resulting in a capital loss of $51,450.04, of which it deducted the $2,000 maximum allowable, and reported a net loss for the year. (R. 9, 18–19, 30.)

The Commissioner determined that the petitioner had a capital gain of $15,075.02 from the sale of the property, with a resultant net income for the year in the amount of $13,170.98, on the basis of which he asserted deficiencies in income and excess profits taxes. (R. 9–11, 18–20, 30.) The difference between the parties was solely as to the petitioner's basis for the property for computation of gain or loss from the sale, the petitioner using the 1932 value, $110,000, while the Commissioner used the basis in the hands of the petitioner's transferor, namely, the 1913 value, $65,041.67. (R. 30–31.)

Before the Board of Tax Appeals, and in the court below, the petitioner claimed that it was entitled to the "stepped-up" basis because the exchange of property for stock did not fall under Section 112 (b) (5) of the Revenue Act of 1932 and hence it was not required to take the transferor's basis under Section 113 (a) (8). In support of its position, the petitioner contended, first, that the exchange was removed from the reach of Section 112 (b) (5) by the transferor's subsequent gifts of stock, and second, in the alternative, that Section 213 (f) of the 1939 Act which made Section 112 (b) (5) applicable notwithstanding the

assumption of indebtedness, was unconstitutional because of its retroactive application. The Board (R. 28–38) and the court below (R. 49–54) rejected both contentions and upheld the Commissioner's use of the transferor's basis.

The first contention has now been abandoned by the petitioner, the sole point made here (Pet. 2) consisting of the attack upon the validity of Section 213 (f) of the 1939 Act.

ARGUMENT

The petitioner acquired the property, subject to the outstanding mortgages which it assumed, solely in exchange for its stock. That exchange clearly falls under Section 112 (b) (5) of the Revenue Act of 1932 (Appendix, *infra,* pp. 9–10), as amended by Section 213 (f) of the 1939 Act (Appendix, *infra,* pp. 13–14), so that the petitioner was required to take the transferor's basis under Section 113 (a) (8) (Appendix, *infra,* p. 11).[3] Holding that petitioner was not entitled to a "stepped-up" basis for the purpose of computing its gain or loss upon sale in 1937, both the Board and the court below correctly rejected the charge, which is repeated here (Pet. 3, 4–7), that Section 213 (f) of the 1939 Act violates the due process clause of the Fifth Amendment when retroactively applied in this case (R. 35–37, 52–54).

[3] Sections 112 (b) (5) and 113 (a) (8) were substantially the same in the 1932 and 1936 Acts.

Congress expressly provided for the retroactive application of Section 213 (f) of the 1939 Act. See *D. W. Klein Co.* v. *Commissioner,* 123 F. (2d) 871 (C. C. A. 7th), certiorari denied, March 16, 1942, and *Commissioner* v. *Corpus Christi T. Co.,* 126 F. (2d) 898 (C. C. A. 5th), in which cases the application of the provisions of Section 213 (f) of the 1939 Act was approved in connection with sales occurring in the years 1932 and 1934, respectively. But the mere retroactivity of a taxing statute is not a valid constitutional objection. See *Brushaber* v. *Union Pac. R. R.,* 240 U. S. 1, 20; *Cooper* v. *United States,* 280 U. S. 409; *Milliken* v. *United States,* 283 U. S. 15; *Welch* v. *Henry,* 305 U. S. 134, 147. In *Cooper* v. *United States, supra,* a retroactive change of the basis of property was held not to be objectionable in the constitutional sense.

Only when, upon consideration of the nature of the change made by the statute, of the circumstances surrounding its enactment and of its practical effect, the statute is shown to be so arbitrary and capricious and lacking in reasonableness as to result in confiscation can the challenged statute be said to offend constitutional limitations. *Brushaber* v. *Union Pac. R. R., supra.* Such is clearly not the case here. In 1937 the petitioner sold the property it had acquired in the 1932 ex-

change. It was not until 1938 that this Court finally decided, in *United States* v. ***Hendler,*** 303 U. S. 564, that under the revenue laws as then drafted the assumption of indebtedness, in what would otherwise be a non-taxable exchange, would result in taxable gain.[4] In order to remove the so-called defect in the revenue laws uncovered by that decision, Congress passed Section 213 (f) in 1939.[5] When the transaction was originally entered into, the transferor, who created the petitioner and acquired all of its stock, did not report the gain from the transaction because he regarded the exchange as a non-taxable one (see R. 16, 22, 36)—under which the petitioner would take over his basis. The effect of the *Hendler* decision in 1938 would have been to change that result, and to make the 1932 exchange a taxable one resulting in gain to the transferor and in a new basis to the petitioner. Section 213 (f) of the 1939 Act removes the effect of that decision,

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[4] Prior thereto, and even prior to the petitioner's sale, there were conflicting decisions on that point. Cf. *Hendler* v. *United States*, 17 F. Supp. 558 (Md.), and *Brons Hotels, Inc.* v. *Commissioner* 34 B. T. A. 376. Hence, there is no basis for the suggestion that petiitoner has had its expectations disappointed. (See R. 53.) Moreover, even if petitioner had actually been disappointed, that would not necessarily compel the conclusion that its rights have been injured in the constitutional sense.

[5] See report of Committee on Ways and Means, H. Rep. No. 855, 76th Cong., 1st Sess., p. 19.

and restores the situation to its original status. Clearly, there is no basis for the suggestion (Pet. 7) of any lack of "fair play."

The gift and estate tax cases cited (Pet. 5–6) by petitioner (*Nichols* v. *Coolidge,* 274 U. S. 531; *Blodgett* v. *Holden,* 275 U. S. 142; *Untermeyer* v. *Anderson,* 276 U. S. 440; *Coolidge* v. *Long,* 282 U. S. 582; *Helvering* v. *Helmholz,* 296 U. S. 93; *White* v. *Poor,* 296 U. S. 98) involve objections not present here. Cf. *Cooper* v. *United States, supra,* pp. 411–412; *Milliken* v. *United States, supra,* pp. 21–22, 23; *Welch* v. *Henry, supra,* p. 147. Here Congress, as a concession to taxpayers, simply provided retroactively for non-taxability of certain exchanges that would otherwise have been taxable under the *Hendler* decision, and as a consequence, there followed a corresponding adjustment in basis under Section 113 (a) (8). The circumstances here are fairly comparable to those in *Welch* v. *Henry, supra,* although less extreme than those present in that case; the legislation herein, to the extent that it required an adjustment in basis, simply closed a loophole and prevented petitioner from obtaining a windfall through the use of an artificially "stepped-up" basis.

CONCLUSION

The decision of the court below is correct and is in accord with the principles established by the applicable decisions of this Court. There is no conflict of decisions. The petition should therefore be denied.

Respectfully submitted.

CHARLES FAHY,
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AUGUST 1942.

APPENDIX

Revenue Act of 1932, c. 209, 47 Stat. 169:

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b), and the loss shall be the excess of such basis over the amount realized.

*   *   *   *   *

(c) *Recognition of Gain or Loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

*   *   *   *   *

SEC. 112. RECOGNITION OF GAIN OR LOSS.

(a) *General Rule.*—Upon the sale or exchange of property the entire amount of the gain or loss, determined under section 111, shall be recognized, except as hereinafter provided in this section.

(b) *Exchanges Solely in Kind:*

*   *   *   *   *

(5) *Transfer to Corporation Controlled by Transferor.*—No gain or loss shall be recognized if property is transferred to a corporation by one or more persons solely in exchange for stock or securities in such corporation, and immediately after the

exchange such person or persons are in control of the corporation; but in the case of an exchange by two or more persons this paragraph shall apply only if the amount of the stock and securities received by each is substantially in proportion to his interest in the property prior to the exchange.

(c) *Gain from Exchanges not Solely in Kind.*—

(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5) of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

*   *   *   *   *

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 111. DETERMINATION OF AMOUNT OF, AND RECOGNITION OF, GAIN OR LOSS.

(a) *Computation of Gain or Loss.*—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 113 (b) for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.

(b) *Amount Realized.*—The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

*   *   *   *   *

SEC. 113. ADJUSTED BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Basis (Unadjusted) of Property.*—The basis of property shall be the cost of such property; except that—

*   *   *   *   *

(8) *Property Acquired by Issuance of Stock or as Paid-in Surplus.*—If the property was acquired after December 31, 1920, by a corporation—

(A) by the issuance of its stock or securities in connection with a transaction described in section 112 (b) (5) (including, also, cases where part of the consideration for the transfer of such property to the corporation was property or money, in addition to such stock or securities), or

(B) as paid-in surplus or as a contribution to capital, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made.

*   *   *   *   *

(14) *Property Acquired before March 1, 1913.*—In the case of property acquired before March 1, 1913, if the basis otherwise determined under this subsection, adjusted (for the period prior to March 1, 1913) as provided in subsection (b), is less than the fair market value of the property as of March 1, 1913, then the basis for determining gain shall be such fair market value. In determining the fair market value of stock in a corporation as of March 1, 1913, due regard shall be given to the fair market value of the assets of the corporation as of that date.

*   *   *   *   *

(b) *Adjusted Basis.*—The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis determined under subsection (a), adjusted as hereinafter provided.

(1) *General Rule.*—Proper adjustment in respect of the property shall in all cases be made—

(A) for expenditures, receipts, losses, or other items, properly chargeable to capital account, including taxes and other carrying charges on unimproved and unproductive real property, but no such adjustment shall be made for taxes or other carrying charges for which deductions have been taken by the taxpayer in determining net income for the taxable year or prior taxable years;

* * * * *

(2) *Substituted Basis.*—The term "substituted basis" as used in this subsection means a basis determined under any provision of subsection (a) of this section or under any corresponding provision of a prior income tax law, providing that the basis shall be determined—

(A) by reference to the basis in the hands of a transferor, donor, or grantor, or

(B) by reference to other property held at any time by the person for whom the basis is to be determined.

Whenever it appears that the basis of property in the hands of the taxpayer is a substituted basis, then the adjustments provided in paragraph (1) of this subsection shall be made after first making in respect of such substituted basis proper adjustments of a similar nature in respect of the period during which the property was held by the trans-

feror, donor, or grantor, or during which the other property was held by the person for whom the basis is to be determined. A similar rule shall be applied in the case of a series of substituted bases.

Revenue Act of 1939, c. 247, 53 Stat. 862:

> SEC. 213. ASSUMPTION OF INDEBTEDNESS.
>
> * * * * *
>
> (f) *Assumption of Liability Not Recognized Under Prior Acts.*—
>
> (1) Where upon an exchange occurring in a taxable year ending after December 31, 1923, and beginning before January 1, 1939, the taxpayer received as part of the consideration property which would be permitted by subsection (b) (4) or (5) of section 112 of the Revenue Act of 1938, or the corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts, to be received without the recognition of gain if it were the sole consideration, and as part of the consideration another party to the exchange assumed a liability of the taxpayer or acquired from the taxpayer property subject to a liability, such assumption or acquisition shall not be considered as "other property or money" received by the taxpayer within the meaning of subsection (c), (d), or (e) of section 112 of the Revenue Act of 1938, or the corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts, and shall not prevent the exchange from being within the provisions of subsection (b) (4) or (5) of section 112 of the Revenue Act of 1938, or the corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts; except that if, in the determination of the tax liability of such taxpayer for the taxable year in which the exchange occurred, by a decision of the

Board of Tax Appeals or of a court which became final before the ninetieth day after the date of enactment of the Revenue Act of 1939, or by a closing agreement, gain was recognized to such taxpayer by reason of such assumption or acquisition of property, then for the purposes of section 112 of the Revenue Act of 1938, and corresponding provisions of the Revenue Act of 1924 or subsequent revenue Acts, such assumption or acquisition (in the amount of the liability considered in computing the gain) shall be considered as money received by the taxpayer upon the exchange.

(2) Paragraph (1) shall be effective with respect to the Revenue Act of 1924 and subsequent revenue Acts as of the date of enactment of each such Act.

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